



**North Carolina Department of Health and Human Services
Division of Mental Health, Developmental Disabilities and Substance Abuse
Services**

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Michael F. Easley, Governor
Carmen Hooker Odom, Secretary
Richard J. Visingardi, Ph.D., Director

February 18, 2002

MEMORANDUM:

TO: Area Directors

FROM: Richard J. Visingardi, Ph.D.

RE: (1) Area Program Withholding for Administrative Costs for
Passthrough Funds
(2) Overview of Settlement Procedures for SFY 02 and Thereafter

Attached is a copy of correspondence from Tom Maynard, Chair of the Management Systems Work Group of the NC Council regarding the method for calculating the administrative rate that area programs may retain when contracting services with providers. In follow-up to the attached request, Division and DHHS Controller Office staff reviewed both the current methodology in use and the Work Group's recommendation. Based on the recommendation of Division and DHHS staff, the current methodology will remain in place until further notice.

In arriving at this decision, the following key factors were considered.

1. I anticipate that the current financing structure will change significantly as we move forward in implementing system reforms. Funding for LME's will most likely be direct funding to accomplish required tasks and not by LME's retaining administrative costs associated with contracted services.
2. Application of the withholding rates only applies to arrangements with contract providers and does not apply to area program provided services. Therefore, fund availability to support area program administrative costs is not strictly limited to those amounts which can be generated through the retention of contract related funding.
3. Previous Medicaid rates were increased by 2% last year to help off-set the loss in administrative revenues due to direct Medicaid billings. The Division has taken this into account by adopting the methodology of dividing the rate by 1.02. This step provides the basis for setting aside the 2% increase to be retained by area programs. Example: If the previous Medicaid rate was \$80, it was increased by \$1.60 (2% of \$80), thereby establishing a new rate of \$81.60. If you divide the new rate of \$81.60 by 1.02, this brings you back to \$80 and provides the full remaining \$1.60 for retention by the area program. The Work Group endorses this step and is not recommending anything different than is currently in place. This methodology applies to both Medicaid rates which were increased by 2% and Division service rates which were increased in concert with the Medicaid change.

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It is after the step outlined in item 3 above, that the Work Group's recommendation differs from current Division practice. The Work Group is recommending that once the rate has been divided by 1.02 as noted above, the resulting amount should be multiplied by 85% to determine the amount for payment to the provider, with the remaining 15% being retained by the area program for administrative costs. EXAMPLE: In a continuation of the above example, once the 2% is retained, this leaves \$80 in the rate. Multiplying that by .85 results in \$68.00 being available to the provider and \$12.00 being retained by the area program. The current methodology for this step which the Division has adopted is to divide the \$80 by 1.15 to arrive at the amount remaining for payment to the provider (\$80 divided by 1.15 = \$69.57), with the balance of \$10.43 being retained by the area program for administration (\$80 minus 69.57 = \$10.43).

The Division adopted this method of computation based on the original instructions set forth in Dr. Baggett's memo of August 18, 1999, and modified slightly in Dr. Robarge's memo of September 21, 2001. When the original methodology for determining the 15% retention by area programs was adopted, it was based on the following formula: Amount paid to the provider times 15% equals the amount which could be billed to Medicaid, not to exceed the Medicaid rate. EXAMPLE: If the amount paid to a provider was \$50 per unit, 15% times the \$50 equals \$7.50 which could be retained by the area program. \$50 plus \$7.50 equals \$57.50, and the \$57.50 was to be billed to Medicaid, provided it did not exceed the Medicaid rate. This allowed area programs to retain a full 15% of the amount being paid to the provider. If one takes the \$57.50 and applies the Work Group's recommended methodology of multiplying that by 85%, this would result in the provider being paid \$48.88 rather than \$50. The basic difference herein is that the Division's original instructions build to the 15% for area administration based on what is actually being paid to the provider and the Work Group's recommendation starts with the actual rate and works down.

The Division's methodology goes back to what was actually being paid to providers and allows for a full 15% retention of that amount, resulting in a slightly higher amount directed into provider services. Therefore, I have elected to retain this methodology. For the sake of clarity, the following is the Division required methodology for the retention of area administration costs from contract providers (assumes an \$81.60 Medicaid rate - which includes the 2% increase adopted last year):

\$81.60	Medicaid rate
\$ 1.60	Area admin retention for 2% (\$81.60 divided by 1.02, subtracted from \$81.60)
\$80.00	Net Balance
\$69.57	Amount to Provider (\$80 divided by 1.15 = \$69.57)
\$10.43	Area admin retention for 15% (\$80 minus \$69.57)
\$12.03	Total Area admin retention (\$1.60 + \$10.43 = \$12.03)

For any Medicaid or Division rates which were not increased by the 2% offset, skip the 2% computation step above and apply only the 15% step.

Associated with the issue of area program retention of funding for administrative costs is the computation of year end settlement to ensure compliance with the Legislative cap of 15% for area administrative costs in SFY 02 and 13% for SFY 03. Regardless of the amount retained by area programs for administrative costs via contract providers and area program administrative costs supported by non-contract related funds, settlement for SFY 02 will limit Division participation to a maximum of 15% for administrative costs. Settlement procedures recommended by the Area Program Administrative Cost Work Group and endorsed by DHHS, will basically be as follows for SFY 02:



A. Determination of Allowable Administrative Costs Amount

Step 1: Determine the total non-administrative expenditures, which will consist of (a) area program expenditures reflected on their books, PLUS (b) sum of payments made to providers billing Medicaid directly for both Medicaid Y-code and CAP-MR.

Step 2: Divide the total non-administrative expenditures by .85 to arrive at the maximum allowable expenditures, inclusive of allowable administrative costs and non-administrative costs.

Step 3: The difference between the .85 division calculation, less the total non-administrative costs equals the maximum allowable administrative costs. Example:

\$1,000,000 Total Area Non-Administrative Expenditures

\$1,176,470 Total Area Non-Administrative Expenditures divided by .85

\$ 176,470 Maximum Allowable Administrative Expenditures *

*Note: \$1,176,470 x 15% also equals \$176,470

Payments of directly billed Medicaid Y-code and CAP-MR services are included since area programs retain an oversight responsibility associated with both types of billings, and this falls within the purview of their administrative responsibilities.

B. Actual Settlement

Area program actual administrative expenditures will be compared to the maximum 15% administrative cap identified per item 5.A. above. Cost related to (1) IPRS and HIPAA implementation and compliance, and (2) the cost of administrative functions provided to outside entities which are supported by receipts will be excluded from consideration as administrative expenditures. An example of item (2) would be: Area program X provides management information system support for area program Y and area program Y pays area program X for this support. Actual costs on area program X's general ledger for the provision of this support would be disregarded in measuring the 15% administrative cost compliance. The amount of actual costs incurred by area program X to provide the service will be defined as the revenues received from area program Y. However, the actual costs on area program Y's general ledger (contract payment to area program X) would be included since the cost relates to their actual administrative functions.

- Area programs with actual administrative costs below the computed 15% maximum cap will be within the allowable limit and no additional settlement action will be needed.
- For area programs with actual administrative costs above the computed 15% maximum cap, the amount above the maximum cap will be handled as follows:
 - If the area program had allowable Division non-Medicaid service units valued at an amount higher than the amount the Division paid for services, excess administrative costs above the 15% maximum will be allowed to be off set against the unreimbursed service units.
 - Any portion of administrative costs above the 15% maximum which cannot be off set against unreimbursed service units described above will be recouped by the Division on a proportionate funding basis. The proportionate funding basis will be: Total Division funding as a percent of total area program costs (total area



program costs will include those booked by the area program plus the sum of payments made to providers billing Medicaid directly for both Medicaid Y-code and CAP-MR).

- Special Note: This methodology addresses compliance with the 15% cap via limiting Division participation in administrative costs. Since area programs are well into the year, the Area Program Administrative Cost Work Group did not believe it was practical to attempt to directly limit area program administrative costs from a budgeting standpoint. The approach of limiting Division participation will, however, have a direct influence on the amount area programs expend for administrative costs.
- SFY 03 and Thereafter: Same as SFY 02, except there will be no provision or allowance to have administrative costs above the computed 13% (drops to 13% in SFY 03) administrative cap off set against unreimbursed service units. The Area Program Administrative Cost Work Group believed this was the general intent of the Special Provision but that area programs could not reasonably adjust budgets until SFY 03 for compliance. For area programs exceeding the computed administrative cap in SFY 03, the Division would recoup, on a proportionate funding basis, its share of excess administrative expenditures as described above.

It is important to understand that retention of area program administrative costs from provider payments and year-end settlement are two different actions. When computing year-end settlements, overall compliance will be governed by the 15% Legislative cap for area administration. Regardless of how administrative costs are funded at the area program level, if area program administrative costs exceed the 15% settlement procedures outlined above, DHHS Controller Office staff will calculate the settlement amount as previously described.

I realize this is a considerable amount of information to absorb and understand. Additional details on the settlement procedures will be distributed later in conjunction with the DHHS Controller's Office. I believe this overview is necessary in order to tie this together with the issue of area program retention of administrative costs from contract providers. Should you have any questions, please contact Phillip Hoffman at 919-733-7013 or e-mail to Phillip.Hoffman@ncmail.net

RJV/ph

Attachment

cc: Area Finance Officer
Lanier Cansler
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